87-36 (1)

No. 87-

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

INVESTMENT COMPANY INSTITUTE and
SECURITIES INDUSTRY ASSOCIATION,

Petitioners,

v.

FEDERAL DEPOSIT INSURANCE CORPORATION, ET AL.,

Respondents.

**PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT**

MATTHEW P. FINK
Senior Vice President and General Counsel
SARAH O'NEIL
Associate General Counsel
INVESTMENT COMPANY INSTITUTE
1600 M Street, N.W.
Suite 600
Washington, D.C. 20036
(202) 293-7700

WILLIAM J. FITZPATRICK
Senior Vice President and General Counsel
DONALD J. CRAWFORD
Senior Vice President and Director of Government Relations
SECURITIES INDUSTRY ASSOCIATION
120 Broadway
New York, New York 10271
(212) 608-1500

Of Counsel

HARVEY L. PITT
(Counsel of Record)
HENRY A. HUBSCHMAN
DAVID M. MILES
FRIED, FRANK, HARRIS, SHRIVER & JACOBSON
(A Partnership Including Professional Corporations)
1001 Pennsylvania Avenue, N.W.
Suite 800
Washington, D.C. 20004-2505
(202) 639-7000

Attorneys for Petitioners Investment Company Institute and Securities Industry Association

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QUESTIONS PRESENTED

1. Where the Glass-Steagall Act expressly prohibits insured nonmember banks from engaging in the mutual fund and securities underwriting businesses "to any extent whatever," and where the Federal Deposit Insurance Act forbids them to engage in activities that are "unsafe and unsound" or "[in]consistent with the purposes" of federal deposit insurance, may the Federal Deposit Insurance Corporation nonetheless authorize more than 9,000 such banks to engage in the prohibited activities through subsidiaries created for that sole purpose and then seek to regulate the conflicts of interest and other abuses that admittedly will result through a self-created scheme of administrative regulation?

2. When Congress adopted the Glass-Steagall Act and the Federal Deposit Insurance Act in the context of longstanding federal common law prohibiting the manipulation of corporate form to defeat federal statutory banking policy, may lower courts except the statutes from this prohibition in the absence of *any* evidence suggesting that Congress intended the exception created?

PARTIES TO THE PROCEEDING

In addition to the petitioners and respondents listed in the caption, the following are also respondents in this action: L. William Seidman, Robert L. Clarke and C. C. Hope.*

*Pursuant to Rule 28.1 of this Court, petitioner Investment Company Institute states that it is the national association of open-end investment companies (commonly known as mutual funds), their investment advisers and their principal underwriters. The Institute has 2,000 mutual fund members with over 29 million shareholders and assets of approximately $785 billion. Pursuant to the same Rule, petitioner Securities Industry Association states that it is a national trade association representing more than 500 securities brokers, dealers and underwriters.

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

Petitioners Investment Company Institute (the "Institute") and Securities Industry Association (the "SIA") respectfully pray that a Writ of Certiorari issue to review the judgment and opinion of the United States Court of Appeals for the District of Columbia Circuit entered in these proceedings on April 7, 1987.

OPINIONS BELOW

The opinion of the United States Court of Appeals for the District of Columbia Circuit (1a-18a)[1] is reported at 815 F.2d 1540. The opinion of the United States District Court for the District of Columbia (39a-44a) is reported at 606 F. Supp. 683. The rule of the Federal Deposit Insurance Corporation ("FDIC") authorizing insured nonmember banks to engage in the securities underwriting and mutual fund businesses through subsidiaries (54a-112a) is reported at 49 Fed. Reg. 46,709 (1984).

1. Citations herein to material printed in Appendix appear as (__ a).

JURISDICTION

The judgment below was entered on April 7, 1987. This Court's jurisdiction is invoked under 28 U.S.C. § 1254(1).

STATUTES INVOLVED

Involved in this action are Section 21 of the Glass-Steagall Act, 12 U.S.C. § 378, and Sections 6 and 8 of the Federal Deposit Insurance Act ("FDIA"), 12 U.S.C. §§ 1816, 1818. The text of these statutes is reprinted in the Statutory Appendix to this brief.[2]

STATEMENT OF THE CASE

A. Background

This case presents the latest effort of federal banking regulators administratively to repeal the flat prohibitions of the Glass-Steagall Act, the primary federal statute governing the basic structure of the financial services industry in this country. The Act is "a prophylactic measure directed against conditions that the experience of the 1920's showed to be great potentials for abuse." *Investment Company Institute* v. *Camp*, 401 U.S. 617, 639 (1971) ("Camp"). Concluding that the securities activities of commercial banks had precipitated the stock market collapse of 1929, the ensuing wave of bank failures and the Great Depression, Congress decided that "drastic" action was in order. *Id.* at 629. Rejecting proposals to permit commercial banks to continue to engage in the securities business subject to ongoing federal supervision and administrative regulation, Congress decided instead to "separat[e] as completely as possible commercial from investment banking." *Board of Governors of the Federal Reserve System* v. *Investment Company Institute*, 450 U.S. 46, 70 (1981) ("Board of Governors").

2. The statutes generally known as the Glass-Steagall Act and the Federal Deposit Insurance Act both were enacted as part of the Banking Act of 1933, 48 Stat. 162, and are codified in various sections of Title 12 of the United States Code.

The statutory barriers Congress erected to achieve this goal are embodied in Sections 16 and 21 of the Act. Section 16 by its terms forbids national banks and member banks to "underwrite" or to deal in "*any* issue of securities or stock." 12 U.S.C. § 24 (Seventh) (emphasis supplied); *see* 12 U.S.C. § 335. Section 21 in turn prohibits "*any* person, firm, corporation, association, business trust, or other similar organization" engaged in the business of "receiving deposits" from engaging at the same time "*to any extent whatever*" in the business of "issuing, underwriting, selling, or distributing . . . stocks, bonds, debentures, notes, or other securities." 12 U.S.C. § 378(a) (emphasis supplied).

As is plain from the sweep of its language, and as this Court itself had declared, the Glass-Steagall Act embodies Congress' considered legislative judgment that "the mere existence of a [bank] securities operation, 'no matter how carefully and conservatively run, is inconsistent with the best interests' of the bank as a whole." *Securities Industry Association* v. *Board of Governors of the Federal Reserve System*, 468 U.S. 137, 157 (1984) ("Becker") (quoting 75 Cong. Rec. 9913 (1932) (remarks of Sen. Bulkley)). The Act reflects Congress' policy determination that, "[w]hen a bank puts itself in competition with securities dealers [and the mutual fund business], the bank must make an accommodation to the kind of ground rules that . . . [cannot] be prudently mixed with the business of commercial banking." *Becker*, 468 U.S. at 155 (quoting *Camp*, 401 U.S. at 637).

B. The FDIC Rule

The Rule at issue has its genesis in the efforts of two insured nonmember banks in 1982 to circumvent the statutory bar by engaging in the mutual fund and securities underwriting businesses through subsidiaries.[3] Concerned over the impact of these "novel" and unprecedented actions upon its statutory obligations

3. The Boston Five Cents Savings Bank ("Boston Five") created two new subsidiary corporations to carry out the mutual fund business on its behalf; Washington Mutual Savings Bank ("Washington Mutual") simply acquired an existing registered securities broker-dealer and its family of registered investment advisers.

under the federal securities laws, the Securities and Exchange Commission ("SEC") requested the FDIC to provide it with a legal opinion stating that the banks' plans did not violate the Glass-Steagall Act (194a-195a).

The FDIC refused.[4] Instead, it issued a generic Policy Statement which abandoned over fifty years of consistent administrative construction and announced that insured nonmember banks may engage in any and all securities activities through subsidiaries to an unlimited extent without running afoul of the Glass-Steagall Act. 47 Fed. Reg. 38,984 (1982); (189a-193a). The Policy Statement thus authorized and encouraged more than 9,000 insured nonmember banks in the nation to follow in the footsteps of Boston Five and Washington Mutual.

At the same time, the FDIC admitted that its Policy Statement created the potential for the very conflicts of interests, financial dangers and other abuses that prompted Congress to enact the Glass-Steagall Act and to exclude insured nonmember banks from the securities business. 47 Fed. Reg. 42,121 (1982); (185a).[5] Rather than enforcing the Congressional remedy of absolute prohibition, however, the FDIC announced its own administrative opinion that the "risks and the conflicts of interest can . . . be adequately addressed by proper regulation." 49 Fed. Reg. at 46,710; (58a).

The agency therefore followed the Policy Statement with rulemaking proceedings designed to cabin the dangers that concededly would flow from the very securities activities the agency

4. The Institute previously had requested the FDIC to issue an opinion concerning the legality of the banks' activities; the FDIC refused that request as well. *See Investment Company Institute* v. *Federal Deposit Insurance Corp.*, 728 F.2d 518 (D.C. Cir. 1984).

5. The FDIC stated that "[the] hazards [contemplated by the Glass-Steagall Act] can and do exist [when a bank is indirectly involved in securities activities]" through subsidiaries. 49 Fed. Reg. 18,497 (1984) (quoting 48 Fed. Reg. 22,155 (1983)); (115a) (brackets in original). Indeed, the agency admitted that the dangers Congress feared are "inherent in [the] involvement of subsidiaries of nonmember banks in securities activities." 47 Fed. Reg. at 38,984; (190a).

had just authorized.[6] The FDIC has admitted that the resulting Rule provides an inadequate substitute for the flat prohibitions of the Glass-Steagall Act, however, since the Rule can only "lessen" the dangers that Congress intended the Act to eliminate in their entirety. 49 Fed. Reg. at 46,711; (61a).

C. The Opinions Below

Because Congress enacted the Glass-Steagall Act to prohibit the precise "commercial bank involvement in marketing securities" the FDIC had authorized, *Becker*, 468 U.S. at 154, the Institute and the SIA brought suit under the Administrative Procedure Act, 5 U.S.C. § 551, *et seq.*, seeking declaratory and injunctive relief from the FDIC's Rule. The United States District Court for the District of Columbia declared itself bound to defer to the agency's statutory construction and upheld the Rule on its merits (39a-44a). The United States Court of Appeals for the District of Columbia Circuit affirmed (1a-18a).

The court of appeals did not dispute that, by prohibiting insured nonmember banks from engaging in the securities underwriting and mutual fund businesses "to any extent whatever," the plain language of the Glass-Steagall Act forbids bank engagement in securities and mutual fund activities through subsidiaries (12a). The court concluded, however, that because Section 20 of the Glass-Steagall Act prohibits *member* banks from being affiliated with any institution "engaged principally" in the securities underwriting business, Section 21 could not prohibit *nonmember* banks from operating securities subsidiaries without rendering Section 20 "meaningless" (15a).

The court also did not dispute that, by forbidding activities that are "unsafe and unsound" or "[in]consistent with the purposes" of federal deposit insurance, the plain language of Sections 6 and 8 of the FDIA prohibits insured nonmember banks from engaging

6. The FDIC issued its Final Rule on November 28, 1984. *See* 49 Fed. Reg. 46,709 (1984); (54a). During the administrative proceedings, the agency issued one Advance Notice of Proposed Rulemaking, *see* 47 Fed. Reg. 42,121 (1982); (184a-188a), and two Proposed Rules, *see* 48 Fed. Reg. 22,155 (1983); (154a-183a), 49 Fed. Reg. 18,497 (1984); (113a-153a).

in the securities underwriting and mutual fund businesses (9a). The court nonetheless determined that, even though "[t]he FDIC itself . . . has recognized that bank subsidiaries . . . engaged in securities activities pose dangers under these two sections," the agency acted "reasonably" when it simply restricted, rather than prohibited, the hazardous activities by subsidiaries (17a).[7]

REASONS FOR GRANTING THE WRIT

A. The Judgment Below Repudiates The Legislative Process And This Court's Decisions In *Camp* And *Becker* By Allowing Bank Regulators To Usurp A Policy Making Role Congress Expressly Reserved For Itself.

The opinion below fundamentally misconceives the role of administrative agencies and courts in effectuating the basic policy decisions Congress has mandated in the financial services arena. In *Board of Governors of the Federal Reserve System* v. *Dimension Financial Corp.*, 106 S. Ct. 681, 689 (1986), this Court unambiguously held that if existing banking statutes do not serve the public interest, "that is a problem for Congress, and not the [banking agencies] or the courts, to address." By sanctioning the FDIC's decision to override the language and legislative purpose of the Glass-Steagall Act and to authorize more than 9,000 banks to engage in the securities business through subsidiaries, the court below turned this basic precept on its head. Action by this Court is necessary not only to reaffirm the primacy of Congress' policy choice to "separat[e] as completely as possible commercial from investment banking," *Board of Governors*, 450 U.S. at 70, but also to preserve Congress' structural decision to reserve

7. The court of appeals initially refused to address the FDIA claim on the grounds that the interests asserted by the Institute and the SIA did not arguably fall within that statute's protected or regulated zone and thus did not confer standing to sue upon them (27a-30a). Following the issuance of this Court's decision in *Clarke* v. *Securities Industry Association*, 107 S. Ct. 750 (1987), however, the court of appeals vacated its original opinion and issued a modified one upholding petitioners' standing under the FDIA and resolving the FDIA claim on its merits (9a-10a).

to itself, rather than to delegate to any agency, the authority and responsibility for making that choice.[8]

First. From 1933 until issuance of its Rule in 1984, the FDIC faithfully applied the plain language of the Glass-Steagall Act and the FDIA to bar insured nonmember banks from participating through subsidiaries in the activities it now has sanctioned. During that time, Congress expressly had considered whether and to what extent Congress should revise the law to permit insured nonmember banks to engage in the mutual fund and securities underwriting businesses.[9] Although Congress in recent years has enacted *other* major reforms to the federal banking laws which have materially altered the existing statutory framework governing financial institutions,[10] Congress has determined not to modify the Glass-Steagall Act's flat prohibitions in the slightest. Rather than deferring to this legislative process, the agency instead intervened and removed from Congressional hands the decision whether, and to what extent, the barriers separating commercial from investment banking should be dismantled.

Second. The FDIC issued the Rule under review not only to further its view of "progressive" banking practices, 49 Fed. Reg.

8. Ironically, the one agency with any experience and expertise in the mutual fund and securities underwriting arena—the SEC—has left no doubt of its view that the Rule "does violence to the intent of the Glass-Steagall Act." *See Shad Dislikes FDIC Securities Proposal*, Daily Rep. for Executives (BNA) No. 111, at A-17 (June 8, 1983) (statement of SEC Chairman Shad). The views of the SEC are entitled to considerable weight here since Congress created the SEC, among other things, to regulate and control transactions in the nation's securities markets in order "to protect . . . and make more effective the national banking system." 15 U.S.C. § 78b.

9. For example, in the last several years, Congress entertained but declined to enact proposed legislation which would have permitted commercial banks to engage in some (but not all) of the activities authorized by the Rule at issue through bank holding company affiliates. *See* S.2181, 98th Cong., 1st Sess. (1983); S.2851, 98th Cong., 2d Sess. (1984); S.60, 100th Cong., 1st Sess. (1987); H.R. 50, 100th Cong., 1st Sess. (1987).

10. *See* Garn-St. Germain Depository Institutions Act of 1982, Pub. L. No. 97-320, 96 Stat. 1469 (1982); Depository Institutions Deregulation and Monetary Control Act of 1980, Pub. L. No. 96-221, 94 Stat. 132 (1980); Financial Institutions Regulatory and Interest Rate Control Act of 1978, Pub. L. No. 95-630, 92 Stat. 3641 (1978).

at 46,710; (59a) but also to create new "profit opportunities" to offset the existing financial difficulties of insured nonmember banks.[11] Apart from thereby arrogating to itself a major policy decision of enormous economic consequence, the FDIC has set in motion forces that may result in the complete realignment of the nation's banking system. Federal banking and securities regulators alike predict that national banks may convert to state charters, state-member banks may abandon their membership in the Federal Reserve System, and banks of all types may dissolve their holding company structures in order to take advantage of the new securities powers that the FDIC, by administrative fiat, has purported to bestow upon insured nonmember banks.[12] Thus, not only is the Rule "tantamount to one of the regulatory players unilaterally changing the rules of the game," *American Bankers Association* v. *Securities & Exchange Commission*, 804 F.2d 739, 755 (D.C. Cir. 1986), but the resulting exercise of "charter

11. *FDIC Securities Proposal and Related Issues: Hearings Before the Subcomm. on Telecommunications, Consumer Protection, and Finance of the House Comm. on Energy and Commerce*, 98th Cong., 1st Sess. 161 (1983) ("FDIC Hearings") (statement of former FDIC Chairman Issac). For many members of the commercial banking industry, these are times of severe financial strain. For example, every year in this decade has witnessed a new record number of bank failures, producing a progressively larger number of banks to have failed in any single year since the Depression. *See, e.g., For Whom The Bell Tolled: A Complete Listing of the 79 U.S. Banks That Bit the Dust in 1984*, Am. Banker, Jan. 15, 1985, at 16; *see Two Commercial Banks Fail, Bringing 1985 Total to 72, FDIC Reports*, 45 Wash. Fin. Rep. (BNA) No. 9, at 311 (Aug. 26, 1985); *Regulators Say Profitability of Banking Industry In Decline, Ask Congress To Help*, 48 Banking Report (BNA) No. 22, at 954 (June 1, 1987) ("Regulators Views"). The trouble segments of the industry include numerous insured nonmember banks with their ranks. *See Regulators Views*, at 954 (Reporting Congressional testimony by FDIC Chairman Seidman that more than 200 banks will fail in 1987, another post-Depression record, and that the number of problem banks on the FDIC's watch-list "has increased to 1,531 with total deposits of $237 billion, at the end of the first quarter [1987], from 1,484 at year-end 1986").

12. *See FDIC Hearings*, at 23, 66 (statement of SEC Chairman Shad); *id.* at 137 (statement of Congressman Wirth); *see also Confusion in the Legal Framework of the American Financial System and Service Industry: Hearings Before a Subcomm. of the House Comm. on Government Operations*, 98th Cong., 1st Sess. 495-96 (1983) ("Barnard Hearings") (statement of Federal Reserve Board General Counsel Michael Bradfield).

swapping" is sure to precipitate "very substantial alterations in the framework of the [nation's] banking system."[13]

Third. This case also presents basic questions concerning the authority of federal administrative agencies to rewrite Acts of Congress wholesale in pursuit of their own policy objectives. In an effort to protect against the financial dangers that admittedly would flow from the activities authorized by its Rule, the FDIC constructed a governing regulatory scheme of legislative magnitude by in effect stitching together pieces of numerous federal statutes, including the federal securities laws, the Federal Reserve Act, and the Bank Holding Company Act, and filling the interstices with a variety of administrative admonitions. In the process, the FDIC not only subjected insured nonmember banks and their subsidiaries to federal statutes Congress never intended to apply to them,[14] but also effectively amended other federal statutes to bring insured nonmember banks, their securities subsidiaries, and other entities within their reach.[15]

The FDIC, however, simply lacks the authority to restructure unilaterally the federal statutory framework governing the nation's banking and securities industries. Federal banking regulators themselves have recognized that the Rule is "of a legislative character" and raises "legislative matters that ought to be

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13. *Barnard Hearings*, at 497 (statement of Federal Reserve Board General Counsel Bradfield); *FDIC Hearings*, at 8-9 (statement of SEC Chairman Shad).

14. To point out just one example, securities subsidiaries of insured nonmember banks now will be subject to the numerous express and implied remedies embodied in the Securities Act of 1933, the Securities Exchange Act of 1934, and the Investment Company Act of 1940 for the protection of investors and investment company shareholders. *See, e.g.*, 15 U.S.C. §§ 77k; 77*l*; 78i; 78j(b); 78q(a); 78r; 80a-29(b); 80a-35(b). These remedies will extend to the banks themselves. *See* 15 U.S.C. §§ 77o; 78t.

15. For example, the FDIC was obligated administratively to "amend" the anti-tying prohibitions of the Bank Holding Company Act to make them applicable to all insured nonmember banks which are not organized in a holding company structure. *See* 49 Fed. Reg. at 46,720; (92a). The FDIC was required to do the same with respect to Section 23A of the Federal Reserve Act, in order to bring securities subsidiaries of insured nonmember banks, as well as mutual funds sponsored or advised by the subsidiaries, within the scope of its lending restrictions. *See* 48 Fed. Reg. at 22,159; (168a).

decided by the Congress under the Constitution and not by regulators."[16] Federal securities regulators in turn have made plain their view that, regardless of questions of power, the FDIC lacks the expertise to exercise such authority. As SEC Chairman Shad has stated, "[a]dministrative action by a single federal agency cannot address the broad implications for all financial service industries, the securities markets and investors and depositors." *FDIC Hearings*, at 6.

Fourth. Unfortunately, the Rule under review does not represent an isolated incident involving a single banking regulator. Rather, under increasing pressure from the institutions they regulate, the federal banking agencies have responded to Congress' refusal to amend the Glass-Steagall Act by simply rewriting it themselves. Thus,

—although the Act prohibits member banks from being affiliated with institutions "principally engaged" in underwriting securities, the Federal Reserve Board has authorized the nation's largest bank holding companies to establish affiliates engaged exclusively in underwriting securities.[17]

—although the Act flatly prohibits banks from selling, distributing or underwriting "bonds," the Comptroller nonetheless has authorized banks to sell, distribute and underwrite bonds which are partially collateralized by mortgages.[18]

—although the Act plainly and unambiguously forbids commercial banks and their affiliates from "selling" any type of securities, the Federal Reserve Board and the Comptroller have each allowed banking organizations subject to

16. *See Barnard Hearings*, at 496 (statement of Federal Reserve Board General Counsel Michael Bradfield).

17. *Order Approving Applications of Citicorp, J.P. Morgan & Co., Inc. and Bankers Trust New York Corporation to Engage in Limited Underwriting and Dealing in Certain Securities*, 73 Fed. Res. Bull. 473 (1987) (*"Underwriting Approvals"*). The Board's order is presently under challenge and has been stayed by the Second Circuit pending completion of judicial review. *Securities Industry Association* v. *Board of Governors of the Federal Reserve System*, No. 87-4041 and consolidated cases (2d Cir.) (Orders of May 19, 1987, May 29, 1987).

18. Comptroller Staff Interpretive Letter No. 362 (May 22, 1986), *reprinted in* [Current] Fed. Banking L. Rep. (CCH) ¶ 85,532, at 77,826.

their jurisdiction to engage in the full service brokerage business.[19]

Moreover, further requests for rulings to engage in securities underwriting activities forbidden by the plain language of the Acts' flat prohibition are pending before the bank regulators.[20] Apart from the litigation these administrative exercises of legislative authority ineluctably generate, efforts to dismantle the Glass-Steagall Act by administrative fiat have triggered a veritable flood of additional revisionist activity and have inflicted serious damage upon the carefully balanced and intertwined statutory scheme Congress legislated to govern the securities and banking industries.[21]

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19. *See National Westminster Bank PLC*, 72 Fed. Res. Bull. 584 (1986), Petition for Review Filed, *Securities Industry Association* v. *Board of Governors of the Federal Reserve System*, No. 86-1412 (D.C. Cir. filed July 14, 1986); Comptroller Staff Interpretive Letter No. 370 (Apr. 16, 1986), *reprinted in* [1985-1987 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,540, at 77,842; *Decision of the Comptroller of the Currency Concerning an Application by American National Bank of Austin, Texas to Establish an Operating Subsidiary to Provide Investment Advice* (Sept. 23, 1983), *reprinted in* [1983-1984 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 99,732, at 87,179; Complaint for Declaratory Judgment and Injunctive and Other Relief Filed, *Securities Industry Association* v. *Conover*, No. 83-3581 (D.D.C. filed Nov. 30, 1983).

20. *See Fed To Consider Requests by 3 Banks for Expanded Underwriting Powers*, Am. Banker, Apr. 22, 1987, at 1 ("Chase [Manhattan Corp.] also has broken new ground in asking the Fed for permission to underwrite mutual funds"). *See also SIA Sues Fed in Second Circuit Over Approval of Section 20 Application*, 48 Banking Rep. (BNA) No. 19, at 850 (May 11, 1987); *Banks Will Seek New Authority From Fed If Securities Applications Are Approved*, 46 Wash. Fin. Rep. (BNA) No. 21, at 893 (May 26, 1986).

21. For example, because Congress understood the Glass-Steagall Act to foreclose banks from engaging in the securities underwriting business, Congress excepted banks from the definition of the terms "broker" and "dealer" in the Securities Exchange Act of 1934. *See* 15 U.S.C. §§ 78c(4), (5). In light of the recent rulings of the federal banking agencies, however, the SEC administratively repealed the exception Congress wrote into the statute. *See* 48 Fed. Reg. 51,930 (1983). The SEC's rule in turn was struck down by the courts, *see American Bankers Association* v. *Securities & Exchange Commission*, 804 F.2d 739 (D.C. Cir. 1986), leaving investors who buy their securities from banks without any of the protections Congress intended when it enacted the federal securities laws to regulate the conduct of securities brokers and dealers.

Action by this Court thus is necessary to reaffirm the judiciary's commitment to the prevention of the piecemeal, administrative dismantling of this fundamental federal statute. If permitted to stand, the decision below will encourage bank regulators to continue assuming policy decisions that may properly be addressed only by Congress. It also inevitably will expand the caseload of the federal judiciary as review of these *ad hoc* administrative efforts to explore and expand the boundaries of the Act is sought. Guidance is needed not only to assist the courts facing these issues, but to reaffirm that lower courts need not and must not sacrifice the language and purpose of the Glass-Steagall Act in deference to whatever excuse offered by the banking regulators seems best designed to rationalize a bank's latest wish to enter the securities underwriting business by some new scheme. *Cf. Florida Lime & Avocado Growers, Inc.* v. *Paul*, 373 U.S. 132, 150-51 (1963).

B. The Judgment Below Eviscerates The Glass-Steagall Act And Tramples The Decisions Of This Court Construing It.

Section 21 expressly makes it unlawful for "any person . . . engaged in the business of issuing, underwriting, selling, or distributing, at wholesale or retail, or through syndicate participation, stocks, bonds, debentures, notes, or other securities, to engage at the same time to any extent whatever in the business of receiving deposits." 12 U.S.C. § 378. By its terms, Section 21 applies to insured nonmember banks, since they engage in the business of "receiving deposits." By its terms, Section 21 also forbids insured nonmember banks to engage in the sanctioned corporate securities underwriting and mutual fund activities, since they involve such banks in the business of "issuing, underwriting, selling, or distributing . . . stocks, bonds, debentures, notes, or other securities." *Becker*, 468 U.S. at 148-49; *Camp*, 401 U.S. at 639. And, by its terms, Section 21 forbids insured nonmember banks to carry on the forbidden activities either directly or through subsidiaries, since the statutory language prohibits banks from engaging in the activities "to any extent

whatever." The Rule simply contravenes the plain language of Section 21.

This Court has directed, moreover, that the "literal terms" of the Glass-Steagall Act are to be applied "as they were written." *Camp*, 401 U.S. at 639; *Board of Governors*, 450 U.S. at 65. Indeed, the Court repeatedly has reiterated that the Act is to be applied in accordance with its "plain language," *Becker*, 468 U.S. at 140; *Securities Industry Association* v. *Board of Governors of the Federal Reserve System*, 468 U.S. 207, 219 (1984) ("Schwab") and is not to be interpreted in a "narrow sense." *Becker*, 468 U.S. at 150. In affirming the FDIC's Rule, the court below simply disregarded these instructions.

It also ignored the underpinnings of the statutory language in the "contemporary legal context" surrounding Congress' enactment of the Glass-Steagall Act. *See Merrill Lynch, Pierce, Fenner & Smith* v. *Curran*, 456 U.S. 353, 378-79 (1982). Established federal common law prohibited then, as it does today, the interposition of a corporation to circumvent a federal statute or to defeat a legislative policy, *United States* v. *Reading Co.*, 253 U.S. 26 (1920); *Chicago, M & St. P. Ry. Co.* v. *Minneapolis Civic & Commerce Association*, 247 U.S. 490 (1918); *United States* v. *Lehigh Valley R. R. Co.*, 220 U.S. 257 (1911), especially in the context of federal banking legislation. *Anderson* v. *Abbott*, 321 U.S. 349 (1944). By legislating against this backdrop, Congress incorporated the precept into the Glass-Steagall Act's flat prohibitions, *Curran*, 456 U.S. at 378-79; *Cannon* v. *University of Chicago*, 441 U.S. 677, 696, 698-99 (1979), thereby confirming that indirect bank securities activities through subsidiaries indeed are prohibited "to any extent whatever." The FDIC simply, and improperly, excepted insured nonmember bank subsidiaries from the statutory bar, even though Congress plainly did not contemplate the exception thus created.

The agency also sacrificed Congress' substantive policy goals and this Court's prior decisions to matters of form and the ingenuity of bank counsel. Regardless of matters of corporate structure, a bank and its securities subsidiary constitute a single

economic entity whose fortunes are inextricably intertwined. It is the *bank* that will create, own, and control its subsidiary, and that will profit or suffer from the subsidiary's success or failure. It is the *bank's* reputation and capital that will stand behind the activities of its subsidiary, and that will rise and fall accordingly. And, it is the *bank* and its depositors that will be exposed to the hazards that prompted Congress to exclude insured nonmember banks from the securities business. Under these circumstances, to dispute that the Rule authorizes insured nonmember *banks* to engage in forbidden securities activities is to ignore economic reality.[22]

The decisions of this Court are in full accord. In *Camp*, for example, the Comptroller of the Currency argued that his ruling authorizing national banks to sponsor mutual funds did not violate Section 21's prohibition against the "issuing" of securities by banks, because the "issuing" would be done by the bank's mutual fund, an entity legally separate and distinct from the bank itself. This Court disagreed. Declaring that the mutual fund was "nothing more than an arm or department of the bank," and that the bank and the fund constituted but one "single entity" for Glass-Steagall purposes, *Camp*, 401 U.S. at 625 n. 12, the Court struck down the Comptroller's ruling. Mutual fund activities,

22. For example, the General Accounting Office concluded in its recent study of bank securities subsidiaries that use of the subsidiaries did not suffice to insulate the banks' deposits from risk or to rebut the market perception that a bank and its securities subsidiary constitute a single economic entity. General Accounting Office, Report to the Chairman, Committee on Banking, Housing and Urban Affairs, U.S. Senate and the Chairman, Committee on Banking, Finance and Urban Affairs, House of Representatives, *Bank Powers: Insulating Banks From The Potential Risks of Expanded Activities* 3-36 (Apr. 1987). These findings are no surprise. Former Citicorp Chairmain Walter Wriston previously has explained that banks and their subsidiaries are so functionally and economically integrated that "[i]t is inconceivable that any major bank would walk away from any subsidiary .... If your name is on the door, all of your capital funds are going to be behind it in the real world. Lawyers can say you have separation, but the marketplace is persuasive, and it would not see it that way." *Business and the Law: Wriston "View" of Banking Bill*, N.Y. Times, Sept. 18, 1984, at D2, col. 1. *Accord FDIC Hearings*, at 43-44 (remarks of SEC Chairman Shad); *id.* at 207 (remarks of E. Gerald Corrigan, President, Federal Reserve Bank of Minneapolis).

the Court held, unlawfully "involve[ ] a *bank* in the underwriting, *issuing,* selling and distributing of securities in violation of §§ 16 and 21 of the Glass-Steagall Act." *Id.* at 639 (emphasis supplied). *See Board of Governors,* 450 U.S. at 65.

In affirming the FDIC's Rule, the court below also trampled the legislative purpose underlying the Glass-Steagall Act. Although the FDIC conceded that permitting insured nonmember banks to engage in the newly authorized activities necessarily will give rise to all the financial dangers, conflicts of interest, and other hazards and abuses that prompted Congress to enact the Glass-Steagall Act, the court of appeals permitted the FDIC to act upon the agency's own view that "the risk and conflicts of interest can . . . be adequately addressed by proper regulation." 49 Fed. Reg. 46,709, 46,710 (1984) (58a). But, when Congress wants to give banking agencies regulatory authority over particular non-banking activities, it knows how to do so and does so expressly. *See* 12 U.S.C. § 1843(c)(8). It did not do so in the Glass-Steagall Act. *Becker*, 468 U.S. at 154.

Indeed, in 1935 Congress expressly refused to permit national banks, "under regulation by the Comptroller of the Currency, to underwrite and sell" various securities, H.R. Conf. Rep. No. 1822, 74th Cong., 1st Sess. 532 (1935), and as recently as 1980 Congress expressly reaffirmed its withholding of any and all regulatory power from the Comptroller with respect to "the securities activities of National Banks under the Act commonly known as the 'Glass-Steagall Act.'" Depository Institution Deregulation and Monetary Control Act of 1980, § 708, 94 Stat. 188 (codified at 12 U.S.C. § 93a). The FDIC simply disregarded this Court's admonitions that "Congress rejected a regulatory approach" when it drafted the Glass-Steagall Act and has adhered to that rejection ever since." *Becker*, 468 U.S. at 153.

The court below refused to give effect to the language or legislative purpose of Section 21 because it believed that to do so would render Section 20 of the Act meaningless (13a-15a). This concern was misplaced. Section 21 by its terms applies to all depository institutions, including insured nonmember banks, *see*

12 U.S.C. § 378(a)(1); *Becker*, 468 U.S. at 148. Section 20, in contrast, applies only to "member bank[s]" and not to the insured nonmember banks the Rule addresses. Straightforward application of Section 21's prohibitions therefore does not render Section 20 "surplusage."

In fact, the structure of the Glass-Steagall Act confirms that Section 21 must be applied in accordance with its plain statutory language; it demonstrates that, when Congress wanted to create exceptions in the Act, or to distinguish between a bank and a separate affiliate corporation, it knew how to do so and did so expressly. *See Becker*, 468 U.S. at 153. For example, notwithstanding the prohibitions of Section 21, Section 20 permits member banks to engage indirectly through affiliates in certain securities activities so long as the affiliates do not "engage[ ]" in them "principally." *See* 12 U.S.C. § 377. Congress, however, inserted no comparable exception for subsidiaries of nonmember banks in Section 21, or in any other provision of the Glass-Steagall Act.[23]

The court below also claimed to find support for the notion that Section 21 does not apply to subsidiaries of insured nonmember banks in floor statements by legislators expressing doubt concerning the power of Congress to exercise federal authority over state-chartered banks not within the Federal Reserve System (14a-15a). These fragments of legislative history, however, have no bearing on the issue presented here. First, other participants in the legislative process expressed a broader view of the scope of federal power.[24] More important, Congress as a whole resolved

23. The court below declined to read Section 20 as an exception to Section 21 because it viewed Section 20's language as solely prohibitory in nature (13a-14a). This reading of the statutory text, however, has been rejected by different panels of the same court and has been renounced by the federal banking regulators. *See Investment Company Institute* v. *Conover*, 790 F.2d 925, 932 (D.C. Cir.), *cert. denied*, 107 S. Ct. 421-22 (1986); *Underwriting Approvals*, 73 Fed. Res. Bull. at 478.

24. *See, e.g., Operation of the National and Federal Reserve Banking System: Hearings Pursuant to S. Res. 71 Before a Subcomm. of the Senate Comm. on Banking and Currency*, 71st Cong., 3d Sess. 482, 490 (1931);

(footnote continued on next page)

the questions concerning the scope of its authority in favor of its broad existence by enacting Section 21 for the express purpose of bringing insured nonmember banks within the reach of the Act's prohibitions.[25] In short, Section 21 means what it says and prohibits insured nonmember banks from engaging in the securities business "to any extent whatever," whether directly or through subsidiaries.[26]

C. The Judgment Below Contravenes The Federal Deposit Insurance Act.

Section 6 of the FDIA commands that the powers of state-chartered banks admitted to the federal deposit insurance system must be "consistent with the purposes of [federal deposit insurance]." 12 U.S.C. § 1816. Section 8 of the FDIA in turn forbids insured nonmember banks to engage in any "unsafe and unsound [banking] practices," upon penalty, among other things, of loss of their deposit insurance. 12 U.S.C. §§ 1818(a), (b). Taken together, these sections are designed to prevent insured nonmember banks from taking:

> any action, or lack of action, which is contrary to generally accepted standards of prudent [banking] operation, the

(footnote continued)
Operation of the National and Federal Reserve Banking Systems: Hearings on S. 4115 Before the Senate Comm. on Banking and Currency, 72d Cong., 1st Sess. 395 (1932).

25. *See* 12 U.S.C. § 378(a)(1) (first proviso); S. Rep. No. 1007, 74th Cong., 1st Sess. 16 (1935) (first proviso relieves state banks from the operation of Section 21(a)(1) of the Banking Act of 1933 to the extent that their securities operations are permitted in the case of national banks and state member banks by Section 16). *Accord* 47 Fed. Reg. at 38,984; (191a) ("Section 21 of the Glass-Steagall Act ... is applicable by its terms to insured nonmember banks.").

26. Moreover, Congress intended the Glass-Steagall Act to encourage, if not pressure, all of the nation's banks to join the Federal Reserve System. *See, e.g.,* 77 Cong. Rec. 3727-28, 3903-04 (remarks of Rep. McGugin), 3907 (remarks of Rep. Lemke), 3909 (remarks of Rep. McFadden), 3911-12 (remarks of Rep. Beedy) (1933). To accept the reasoning of the court of appeals is to conclude that, despite this goal, Congress at the same time created enormous incentives for insured nonmember banks to remain outside the system by exempting their subsidiaries from the Glass-Steagall Act's prohibitions.

> possible consequences of which, if continued, would be abnormal risk or loss or damage to an institution, its shareholders, or the agencies administering the insurance funds.[27]

There can be no question that the securities activities authorized by the Rule contravene prudent banking standards and pose an abnormal risk of loss to insured nonmember banks. Indeed, it is precisely because these activities are so "destructive of prudent and disinterested commercial banking" and so potentially "devastating to the solvency of . . . commercial banks" that Congress forbade the activities to insured nonmember banks in the first place. *Becker*, 468 U.S. at 145, 155 (quoting *Camp*, 401 U.S. at 634). And, while the court below affirmed the FDIC's policy judgment that the Rule's securities activities are not *per se* unsafe and unsound, that determination is "squarely at odds with the congressional judgment" made over 50 years ago. *FDIC Hearings*, at 70 (statement of SEC Commissioner Longstreth). As this Court has declared, Congress itself concluded "*that the mere existence of a securities operation, 'no matter how carefully and conservatively run,' is inconsistent with the best interests' of the bank as whole.*" *Becker*, 468 U.S. at 157 (emphasis supplied) (quoting 75 Cong. Rec. 9913 (1932)).

In truth, it is simply untenable to argue that Congress considered the activities authorized by the Rule to be anything other than *per se* unsafe and unsound and completely inconsistent with the purpose of federal deposit insurance. The Glass-Steagall Act and the FDIA both were enacted as part of the Banking Act of 1933, both were considered by the same committees and passed by the same Congress, and both were designed to restore public confidence in the nation's shattered banking system. *Cf. Becker*,

27. *See Gulf Federal Savings & Loan Association* v. *Federal Home Loan Bank Board*, 651 F.2d 259, 264 (5th Cir. 1981) (quoting 112 Cong. Rec. 26,474 (1966) (remarks of Chairman Horn)), *cert. denied*, 458 U.S. 1121 (1982). *Accord First National Bank* v. *Smith*, 610 F.2d 1258 (5th Cir. 1980); *Independent Bankers Association* v. *Heimann*, 613 F.2d 1164, 1168-69 (D.C. Cir. 1979), *cert. denied*, 449 U.S. 823 (1980); *First National Bank* v. *Department of the Treasury*, 568 F.2d 610, 611 n.2 (8th Cir. 1978).

468 U.S. at 145-48. To heed the arguments accepted by the court below, therefore, is to conclude that, while Congress intended in one part of the Banking Act of 1933 to exclude insured nonmember banks from the mutual fund and the securities underwriting business because of their enormous and inherent financial dangers, Congress nonetheless intended in another part of the Act to provide federal deposit insurance to banks which endanger their deposits by engaging in the forbidden activities. To state the proposition is to refute it.[28]

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28. Ironically, ever since the FDIC authorized the securities activities presently under review, the agency has pressed Congress for legislation to restructure and bolster the federal deposit insurance funds. *See* Federal Deposit Insurance Corporation, *Deposit Insurance In A Changing Environment* (Apr. 15, 1983); Federal Deposit Insurance Corporation, *1983 Annual Report* xi ("*1983 Annual Report*"). *See also FDIC Submits Revised Deposit Insurance Reform Bill*, 44 Wash. Fin. Rep. (BNA) No. 13, at 562 (Apr. 1, 1985); *Regulators Views*, at 954-55. Thus, the FDIC warned that "[s]triking changes in the competitive environment for financial institutions have made it clear that the mechanisms crafted to regulate and insure them half a century ago no longer are appropriate and that change can no longer be delayed." *1983 Annual Report*, at x. . These changes in the competitive environment, of course, include not only the banking "deregulation" the agency has brought about in its rule, but also the "post-Depression record" number of bank failures to which the agency's rule ultimately may contribute. *See id.*

CONCLUSION

For each and all of the reasons set forth above, the requested Writ of Certiorari should issue.

Respectfully submitted,

/s/ HARVEY L. PITT

HARVEY L. PITT
(*Counsel of Record*)
HENRY A. HUBSCHMAN
DAVID M. MILES
FRIED, FRANK, HARRIS, SHRIVER & JACOBSON
(A Partnership Including Professional Corporations)
1001 Pennsylvania Avenue, N.W.
Suite 800
Washington, D.C. 20004-2505
(202) 639-7000

Attorneys for Petitioners Investment Company Institute and Securities Industry Association

MATTHEW P. FINK
Senior Vice President and General Counsel
SARAH O'NEIL
Assistant General Counsel
INVESTMENT COMPANY INSTITUTE
1600 M Street, N.W.
Suite 600
Washington, D.C. 20036
(202) 293-7700

WILLIAM J. FITZPATRICK
Senior Vice President and General Counsel
DONALD J. CRAWFORD
Senior Vice President and Director of Government Relations
SECURITIES INDUSTRY ASSOCIATION
120 Broadway
New York, New York 10271
(212) 608-1500

Of Counsel

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STATUTORY APPENDIX

Section 21 of the Glass-Steagall Act, 12 U.S.C. § 378(a)(1), provides in pertinent part:

> [I]t shall be unlawful * * * [f]or any person, firm, corporation, association, business trust, or other similar organization, engaged in the business of issuing, underwriting, selling, or distributing, at wholesale or retail, or through syndicate participation, stocks, bonds, debentures, notes, or other securities, to engage at the same time to any extent whatever in the business of receiving deposits subject to check or to repayment upon presentation of a passbook, certificate of deposit, or other evidence of debt, or upon request of the depositor: *Provided*, That the provisions of this paragraph shall not prohibit national banks or State banks or trust companies (whether or not members of the Federal Reserve System) or other financial institutions or private bankers from dealing in, underwriting, purchasing, and selling investment securities, or issuing securities, to the extent permitted to national banking associations by the provisions of section 24 of this title * * *.

Section 6 of the Federal Deposit Insurance Act, 12 U.S.C. § 1816, provides as follows:

> The factors to be enumerated in the certificate required under section 1814 of this title and to be considered by the Board of Directors under section 1815 of this title shall be the following: The financial history and condition of the bank, the adequacy of its capital structure, its future earnings prospects, the general character of its management, the convenience and needs of the community to be served by the bank, and whether or not its corporate powers are consistent with the purposes of this chapter.

Section 8(a) of the Federal Deposit Insurance Act, 12 U.S.C. § 1818(a), provides in pertinent part:

> Any insured bank * * * may, upon not less than ninety days' written notice to the Corporation, terminate its status as an insured bank. Whenever the Board of Directors shall find that an insured bank or its directors or trustees have engaged or are engaging in unsafe or unsound practices in conducting the business of such bank, or is in an

unsafe or unsound condition to continue operations as an insured bank, or violated an applicable law, rule, regulation or order, or any condition imposed in writing by the Corporation in connection with the granting of any application or other request by the bank, or any written agreement entered into with the Corporation, the Board of Directors shall first give to the Comptroller of the Currency in the case of a national bank or a district bank, to the Federal Home Loan Bank Board in the case of an insured Federal savings bank, to the authority having supervision of the bank in the case of a State Bank, and to the Board of Governors of the Federal Reserve System in the case of a State member bank, a statement with respect to such practices or violations for the purpose of securing the correction thereof and shall give a copy thereof to the bank. Unless such correction shall be made within one hundred and twenty days, or such shorter period not less than twenty days fixed by the Corporation in any case where the Board of Directors in its discretion has determined that the insurance risk of the Corporation is unduly jeopardized, or fixed by the Comptroller of the Currency in the case of a national bank, or the Federal Home Loan Bank Board in the case of an insured Federal savings bank, or the State authority in the case of a State bank, or Board of Governors of the Federal Reserve System in the case of a State member bank as the case may be, the Board of Directors, if it shall determine to proceed further, shall give to the bank not less than thirty days' written notice of intention to terminate the status of the bank as an insured bank, and shall fix a time and place for a hearing before the Board of Directors or before a person designated by it to conduct such hearing, at which evidence may be produced, an upon such evidence the Board of Directors shall make written findings which shall be conclusive. If the Board of Directors shall find that any unsafe or unsound practice or condition or violation specified in such statement has been established and has not been corrected within the time above prescribed in which to make such corrections, the Board of Directors may order that the insured status of the bank be terminated on a date subsequent to such finding and to the expiration of the time specified in such notice of intention.

Section 8(b)(1) of the Federal Deposit Insurance Act, 12 U.S.C. § 1818(b)(1), provides in pertinent part:

> If, in the opinion of the appropriate Federal banking agency, any insured bank, bank which has insured deposits, or any director, officer, employee, agent, or other person participating in the conduct of the affairs of such a bank is engaging or has engaged, or the agency has reasonable cause to believe that the bank or any director, officer, employee, agent, or other person participating in the conduct of the affairs of such bank is about to engage, in an unsafe or unsound practice in conducting the business of such bank, or is violating or has violated, or the agency has reasonable cause to believe that the bank or any director, officer, employee, agent, or other person participating in the conduct of the affairs of such bank is about to violate, a law, rule, or regulation, or any condition imposed in writing by the agency in connection with the granting of any application or other request by the bank or any written agreement entered into with the agency, the agency may issue and serve upon the bank or such director, officer, employee, agent, or other person a notice of charges in respect thereof. The notice shall contain a statement of the facts constituting the alleged violation or violations or the unsafe or unsound practice or practices, and shall fix a time and place at which a hearing will be held to determine whether an order to cease and desist therefrom should issue against the bank or the director, officer, employee, agent, or other person participating in the conduct of the affairs of such bank. Such hearing shall be fixed for a date not earlier than thirty days nor later than sixty days after service of such notice unless an earlier or a later date is set by the agency at the request of any party so served. Unless the party or parties so served shall appear at the hearing personally or by a duly authorized representative, they shall be deemed to have consented to the issuance of the cease-and-desist order. In the event of such consent, or if upon the record made at any such hearing, the agency shall find that any violation or unsafe or unsound practice specified in the notice of charges has been established, the agency may issue and serve upon the bank or the director, officer, employee, agent, or other person participating in the conduct of the affairs of such

bank an order to cease and desist from any such violation or practice. Such order may, by provisions which may be mandatory or otherwise, require the bank or its directors, officers, employees, agents, and other persons participating in the conduct of the affairs of such bank to cease and desist from the same, and, further, to take affirmative action to correct the conditions resulting from any such violation or practice.